CHS INC
Form 10-K/A
January 21, 2004

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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K/A-1

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Fiscal Year Ended August 31, 2003

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to .

Commission file number: 0-50150

CHS Inc.

(Exact name of registrant as specified in its charter)

Minnesota *(State or other jurisdiction of incorporation or organization)*	**41-0251095** *(I.R.S. Employer Identification Number)*
5500 Cenex Drive **Inver Grove Heights, Minnesota 55077** *(Address of principal executive office, including zip code)*	**(651) 355-6000** *(Registrant s Telephone number, including area code)*

Securities Registered Pursuant to Section 12(b) of the Act:
None
Securities Registered Pursuant to Section 12(g) of the Act:
8% Cumulative Redeemable Preferred Stock
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K: o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant s most recently completed second fiscal quarter:

The registrant s voting and non-voting common equity has no market value (the registrant is a member cooperative).

Indicate the number of shares outstanding of each of the registrant s classes of common stock, as of the latest practicable date: The registrant has no common stock outstanding.

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None.

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PART I.

Item 1. ***Business***

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

The information in this Annual Report on Form 10-K for the year ended August 31, 2003, includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to the Company. In addition, the Company and its representatives and agents may from time to time make other written or oral forward-looking statements, including statements contained in the Company s filings with the Securities and Exchange Commission and its reports to its members and securityholders. Words and phrases such as will likely result, are expected to, will continue, is anticipated, estimate, project and similar expressions identify forward-looking statements. The Co wishes to caution readers not to place undue reliance on any forward-looking statements, which speak only as of the date made.

The Company s forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those discussed in the forward-looking statements. This Cautionary Statement is for the purpose of qualifying for the safe harbor provisions of the Act and is intended to be a readily available written document that contains factors which could cause results to differ materially from those projected in the forward-looking statements. The following matters, among others, may have a material adverse effect on the business, financial condition, liquidity, results of operations or prospects, financial or otherwise, of the Company. Reference to this Cautionary Statement in the context of a forward-looking statement shall be deemed to be a statement that any one or more of the following factors may cause actual results to differ materially from those which might be projected, forecasted, estimated or budgeted by the Company in the forward-looking statement or statements.

The following factors are in addition to any other cautionary statements, written or oral, which may be made or referred to in connection with any particular forward-looking statement. The following review should not be construed as exhaustive.

The Company undertakes no obligation to revise any forward-looking statements to reflect future events or circumstances.

OUR REVENUES AND OPERATING RESULTS COULD BE ADVERSELY AFFECTED BY CHANGES IN COMMODITY PRICES. Our revenues and earnings are affected by market prices for commodities such as crude oil, natural gas, grain, oilseeds, and flour. Commodity prices generally are affected by a wide range of factors beyond our control, including the weather, disease, insect damage, drought, the availability and adequacy of supply, government regulation and policies, and general political and economic conditions. We are also exposed to fluctuating commodity prices as the result of our inventories of commodities, typically grain and petroleum products, and purchase and sale contracts at fixed or partially fixed prices. At any time, our inventory levels and unfulfilled fixed or partially fixed price contract obligations may be substantial. Increases in market prices for commodities that we purchase without a corresponding increase in the prices of our products or our sales volume or a decrease in our other operating expenses could reduce our revenues and net income.

In our energy operations, profitability depends largely on the margin between the cost of crude oil that we refine and the selling prices that we obtain for our refined products. Prices for both crude oil and for gasoline, diesel fuel, and other refined petroleum products fluctuate widely. Factors influencing these prices, many of which are beyond our control, include:

- levels of worldwide and domestic supplies;
- capacities of domestic and foreign refineries;
- the ability of the members of OPEC to agree to and maintain oil price and production controls, and the price and level of foreign imports generally;

- political instability or armed conflict in oil-producing regions;
- the level of consumer demand;
- the price and availability of alternative fuels;
- the availability of pipeline capacity; and
- domestic and foreign governmental regulations and taxes.

The long-term effects of these and other conditions on the prices of crude oil and refined petroleum products are uncertain and ever-changing. Accordingly, we expect our margins on and the profitability of our energy business to fluctuate, possibly significantly, over time.

OUR OPERATING RESULTS COULD BE ADVERSELY AFFECTED IF OUR MEMBERS WERE TO DO BUSINESS WITH OTHERS RATHER THAN WITH US. We do not have an exclusive relationship with our members and our members are not obligated to supply us with their products or purchase products from us. Our members often have a variety of distribution outlets and product sources available to them. If our members were to sell their products to other purchasers or purchase products from other sellers, our revenues would decline and our results of operations could be adversely affected.

WE PARTICIPATE IN HIGHLY COMPETITIVE BUSINESS MARKETS IN WHICH WE MAY NOT BE ABLE TO CONTINUE TO COMPETE SUCCESSFULLY. We operate in several highly competitive business segments and our competitors may succeed in developing new or enhanced products that are better than ours, and may be more successful in marketing and selling their products than we are with ours. Competitive factors include price, service level, proximity to markets, product quality and marketing. In some of our business segments, such as Energy, we compete with companies that are larger, better known and have greater marketing, financial, personnel and other resources. As a result, we may not be able to continue to compete successfully with our competitors.

CHANGES IN FEDERAL INCOME TAX LAWS OR IN OUR TAX STATUS COULD INCREASE OUR TAX LIABILITY AND REDUCE OUR NET INCOME. Current federal income tax laws, regulations and interpretations regarding the taxation of cooperatives, which allow us to exclude income generated through business with or for a member (patronage income) from our taxable income, could be changed. If this occurred, or if in the future we were not eligible to be taxed as a cooperative, our tax liability would significantly increase and our net income significantly decrease.

WE INCUR SIGNIFICANT COSTS IN COMPLYING WITH APPLICABLE LAWS AND REGULATIONS. ANY FAILURE TO MAKE THE CAPITAL INVESTMENTS NECESSARY TO COMPLY WITH THESE LAWS AND REGULATIONS COULD EXPOSE US TO FINANCIAL LIABILITY. We are subject to numerous federal, state and local provisions regulating our business and operations and we incur and expect to incur significant capital and operating expenses to comply with these laws and regulations. We may be unable to pass on those expenses to customers without experiencing volume and margin losses. For example, capital expenditures for upgrading our refineries, largely to comply with regulations requiring the reduction of sulfur levels in refined petroleum products, are expected to be approximately $87.0 million for our Laurel, Montana refinery and $324.0 million for National Cooperative Refinery Association s McPherson, Kansas refinery, of which $8.7 million had been spent at the Laurel refinery and $36.5 million had been spent by NCRA at the McPherson refinery as of August 31, 2003. We expect all of these compliance capital expenditures at the refineries to be complete by December 31, 2005, and anticipate funding these projects with a combination of cash flows from operations and debt proceeds.

We establish reserves for the future cost of meeting known compliance obligations, such as remediation of identified environmental issues. However, these reserves may prove inadequate to meet our actual liability. Moreover, amended, new or more stringent requirements, stricter interpretations of existing requirements or the future discovery of currently unknown compliance issues may require us to make material expenditures or subject us to liabilities that we currently do not anticipate. Furthermore, our

failure to comply with applicable laws and regulations could subject us to administrative penalties and injunctive relief, civil remedies including fines and injunctions, and recalls of our products.

ENVIRONMENTAL LIABILITIES COULD ADVERSELY AFFECT OUR RESULTS AND FINANCIAL CONDITION. Many of our current and former facilities have been in operation for many years and, over that time, we and other operators of those facilities have generated, used, stored and disposed of substances or wastes that are or might be considered hazardous under applicable environmental laws, including chemicals and fuels stored in underground and above-ground tanks. Any past or future actions in violation of applicable environmental laws could subject us to administrative penalties, fines and injunctions. Moreover, future or unknown past releases of hazardous substances could subject us to private lawsuits claiming damages and to adverse publicity.

ACTUAL OR PERCEIVED QUALITY, SAFETY OR HEALTH RISKS ASSOCIATED WITH OUR PRODUCTS COULD SUBJECT US TO LIABILITY AND DAMAGE OUR BUSINESS AND REPUTATION. If any of our food or feed products became adulterated or misbranded, we would need to recall those items and could experience product liability claims if consumers were injured as a result. A widespread product recall or a significant product liability judgment could cause our products to be unavailable for a period of time or a loss of consumer confidence in our products. Even if a product liability claim is unsuccessful or is not fully pursued, the negative publicity surrounding any assertion that our products caused illness or injury could adversely affect our reputation with existing and potential customers and our corporate and brand image. Moreover, claims or liabilities of this sort might not be covered by our insurance or by any rights of indemnity or contribution that we may have against others. In addition, general public perceptions regarding the quality, safety or health risks associated with particular food or feed products, such as the concern in some quarters regarding genetically modified crops, could reduce demand and prices for some of the products associated with our businesses. To the extent that consumer preferences evolve away from products that our members or we produce for health or other reasons, such as the growing demand for organic food products, and we are unable to develop products that satisfy new consumer preferences, there will be a decreased demand for our products.

OUR OPERATIONS ARE SUBJECT TO BUSINESS INTERRUPTIONS AND CASUALTY LOSSES; WE DO NOT INSURE AGAINST ALL POTENTIAL LOSSES AND COULD BE SERIOUSLY HARMED BY UNEXPECTED LIABILITIES. Our operations are subject to business interruptions due to unanticipated events such as explosions, fires, pipeline interruptions, transportation delays, equipment failures, crude oil or refined product spills, inclement weather and labor disputes. For example:

- our oil refineries and other facilities are potential targets for terrorist attacks that could halt or discontinue production;
- our inability to negotiate acceptable contracts with unionized workers in our operations could result in strikes or work stoppages; and
- the significant inventories that we carry could be damaged or destroyed by catastrophic events, extreme weather conditions or contamination.

We maintain insurance against many, but not all, potential losses or liabilities arising from these operating hazards, but uninsured losses or losses above our coverage limits are possible. Uninsured losses and liabilities arising from operating hazards could have a material adverse effect on our financial position or results of operations.

OUR COOPERATIVE STRUCTURE LIMITS OUR ABILITY TO ACCESS EQUITY CAPITAL. As a cooperative, we may not sell common equity in our company. In addition, existing laws and our articles of incorporation and bylaws contain limitations on dividends of 8% of any preferred stock that we may issue. These limitations restrict our ability to raise equity capital and may adversely affect our ability to compete with enterprises that do not face similar restrictions.

CONSOLIDATION AMONG THE PRODUCERS OF PRODUCTS WE PURCHASE AND CUSTOMERS FOR PRODUCTS WE SELL COULD ADVERSELY AFFECT OUR REVENUES AND OPERATING

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RESULTS. Consolidation has occurred among the producers of products we purchase, including crude oil and grain, and is likely to continue in the future. Consolidation could increase the price of these products and allow suppliers to negotiate pricing and other contract terms that are less favorable to us. Consolidation also may increase the competition among consumers of these products to enter into supply relationships with a smaller number of producers resulting in potentially higher prices for the products we purchase.

Consolidation among purchasers of our products and in wholesale and retail distribution channels has resulted in a smaller customer base for our products and intensified the competition for these customers. For example, ongoing consolidation among distributors and brokers of food products and food retailers has altered the buying patterns of these businesses, as they have increasingly elected to work with product suppliers who can meet their needs nationwide rather than just regionally or locally. If these distributors, brokers, and retailers elect not to purchase our products, our sales volumes, revenues, and profitability could be significantly reduced.

IF OUR CUSTOMERS CHOSE ALTERNATIVES TO OUR REFINED PETROLEUM PRODUCTS OUR REVENUES AND PROFITS MAY DECLINE. Numerous alternative energy sources currently under development that could serve as alternatives to our gasoline, diesel fuel and other refined petroleum products. If any of these alternative products become more economically viable or preferable to our products for environmental or other reasons, demand for our energy products would decline. Demand for our gasoline, diesel fuel and other refined petroleum products also could be adversely affected by increased fuel efficiencies.

OUR AGRONOMY BUSINESS IS DEPRESSED AND COULD CONTINUE TO UNDERPERFORM IN THE FUTURE. Demand for agronomy products in general has been adversely affected in recent years by drought and poor weather conditions, idle acreage and development of insect and disease-resistant crops. These factors could cause Agriliance, LLC, an agronomy marketing and distribution venture in which we own a minority interest, to be unable to operate at profitable margins. In addition, these and other factors, including fluctuations in the price of natural gas and other raw materials, an increase in recent years in domestic and foreign production of fertilizer, and intense competition within the industry, in particular from lower-cost foreign producers, have created particular pressure on producers of fertilizers. As a result, CF Industries, Inc., a fertilizer manufacturer in which we hold a minority cooperative interest, has suffered significant losses in recent years as it has incurred increased prices for raw materials but has been unable to pass those increased costs on to its customers.

TECHNOLOGICAL IMPROVEMENTS IN AGRICULTURE COULD DECREASE THE DEMAND FOR OUR AGRONOMY PRODUCTS. Technological advances in agriculture could decrease the demand for crop nutrients, and other crop input products and services that we provide. Genetically engineered seeds that resist disease and insects or meet certain nutritional requirements could affect the demand for our crop nutrients and crop protection products, as well as the demand for fuel that we sell and which is used to operate application equipment relating to these products.

WE OPERATE SOME OF OUR BUSINESS THROUGH JOINT VENTURES IN WHICH OUR RIGHTS TO CONTROL BUSINESS DECISIONS ARE LIMITED. Several parts of our business, including in particular our agronomy business segment and portions of our grain marketing, wheat milling and foods businesses, are operated through joint ventures with unaffiliated third parties. By operating a business through a joint venture, we have less control over business decisions than we have in our wholly owned businesses. In particular, we generally cannot act on major business initiatives in our joint ventures without the consent of the other party or parties in that venture.

THE COMPANY

CHS Inc. (CHS or the Company) is one of the nation s leading integrated agricultural companies. As a cooperative, the Company is owned by farmers and ranchers and their local cooperatives from the Great Lakes to the Pacific Northwest and from the Canadian border to Texas. CHS buys commodities from and

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provides products and services to its members and other customers. The Company provides a wide variety of products and services, from initial agricultural inputs such as fuels, farm supplies, crop nutrients and crop protection products, to agricultural outputs that include grains and oilseeds, grain and oilseed processing and food products. A portion of the Company s operations are conducted through equity investments and joint ventures whose operating results are not fully consolidated with the Company s results; rather, a proportionate share of the income or loss from those entities is included as a component in the Company s net income under the equity method of accounting. For the fiscal year ended August 31, 2003, the Company s total revenues were $9.4 billion.

The Company s operations are organized into five business segments: Agronomy, Energy, Country Operations and Services, Grain Marketing and Processed Grains and Foods. Together these business segments create vertical integration to link producers with consumers. The first two segments, Agronomy and Energy, produce and provide for the wholesale distribution of inputs that are essential for crop production. The third segment, Country Operations and Services, serves as the Company-owned retailer of a portion of these crop inputs and also serves as the first handler of a significant portion of the crops marketed and processed by the Company. The fourth segment, Grain Marketing, purchases and resells grains and oilseeds originated by the Country Operations and Services segment, by member cooperatives and also by third parties. The fifth business segment, Processed Grains and Foods, converts grains and oilseeds into value-added products.

Only producers of agricultural products and associations of producers of agricultural products may be members of CHS. The Company s earnings derived from business conducted with these members are allocated to members based on the volume of business they do with the Company. Members receive earnings in the form of patronage refunds (which are also called patronage dividends) in cash and patron s equities, which may be redeemed over time. Earnings derived from non-members are taxed at regular corporate rates and are retained by the Company as unallocated equity. The Company also receives patronage refunds from the cooperatives in which it is a member if those cooperatives have earnings to distribute and the Company qualifies for patronage refunds from them.

The origins of CHS date back to the early 1930s with the founding of the predecessor companies of Cenex, Inc. and Harvest States Cooperatives. CHS emerged as the result of the merger of the two entities in 1998, and is headquartered in Inver Grove Heights, Minnesota. In August 2003, the Company changed its name from Cenex Harvest States Cooperatives to CHS Inc.

The international sales information and segment information in Notes 2 and 11 to the consolidated financial statements are incorporated by reference into the following business segment descriptions.

The business segment financial information presented below does not represent the results that would have been obtained had the relevant business segment been operated as an independent business.

AGRONOMY

Overview

Through the Agronomy business segment, the Company is engaged in the manufacture of crop nutrients and the wholesale distribution of crop nutrients and crop protection products. The Company conducts its agronomy operations primarily through two investments a 20% cooperative ownership interest in CF Industries, Inc. (CF Industries) and, effective January 2000, a 25% ownership interest in Agriliance, LLC (Agriliance). CF Industries manufactures crop nutrient products, particularly nitrogen and phosphate fertilizers, and is one of the largest suppliers to Agriliance. Agriliance is one of North America s largest wholesale distributors of crop nutrients, crop protection products and other agronomy products based on sales.

There is significant seasonality in the sale of crop nutrients and crop protection products and services, with peak activity coinciding with the planting and input seasons.

The Company s minority ownership interests in CF Industries and Agriliance are treated as investments, and therefore, those entities revenues and expenses are not reflected in the Company s operating results. CF Industries is treated as a cost method investment and Agriliance is treated as an equity method investment. CF Industries and Agriliance each have their own line of financing, without recourse to the Company.

Operations

CF Industries. CF Industries is an interregional agricultural cooperative involved in the manufacturing of crop nutrient products. It is one of North America s largest producers of nitrogen and phosphate fertilizers based on plant capacity. Through its members, CF Industries nitrogen and phosphate fertilizer products reach farmers and ranchers in 48 states and two Canadian provinces. CF Industries conducts its operations primarily from the following facilities:

a nitrogen manufacturing and processing facility at Donaldsonville, Louisiana;

a phosphate mine and phosphate fertilizer plant in central Florida; and

a 66% ownership interest in a nitrogen fertilizer manufacturing and processing facility in Alberta, Canada.

Agriliance. Agriliance is the one of the nation s largest wholesale distributors of crop nutrients (fertilizers) and crop protection products (insecticides, fungicides and pesticides) based on sales, accounting for an estimated 19% of the U.S. market for crop nutrients and approximately 26% of the U.S. market for crop protection products. As a wholesale distributor, Agriliance has warehouse, distribution and service facilities located throughout the country. Agriliance also owns and operates retail agricultural units in the southern United States. Agriliance purchased approximately 36% of its fertilizer from CF Industries during fiscal year 2003, and purchases most of its crop protection products from Monsanto and Sygenta.

Agriliance was formed in 2000 when CHS, Farmland Industries Inc. (Farmland) and Land O Lakes, Inc. (Land O Lakes) contributed their respective agronomy businesses to the new company in consideration for ownership interests (25% each for CHS and Farmland and 50% for Land O Lakes) in the venture. CHS and Farmland hold their interests in Agriliance through United Country Brands, LLC, a 50/50 jointly-owned holding company.

In April, 2003, CHS acquired a 13.1% additional economic interest in the crop protection products business of Agriliance (the CPP Business) for a cash payment of $34.3 million. After the transaction, the economic interests in Agriliance are owned 50% by Land O Lakes, 25% plus an additional 13.1% of the CPP Business by CHS and 25% less 13.1% of the CPP Business by Farmland. The ownership or governance interests in Agriliance did not change with the purchase of this additional economic interest. Agriliance s earnings are split among the members based upon the respective economic interests of each member.

Products and Services

CF Industries manufactures crop nutrient products, primarily nitrogen and phosphate fertilizers and potash. Agriliance wholesales crop nutrient products and crop protection products that include insecticides, fungicides, and pesticides. Agriliance also provides field and technical services, including soil testing, adjuvant and herbicide formulation, application and related services.

Sales and Marketing; Customers

CF Industries sells its crop nutrient products to large agricultural cooperatives and distributors. Its largest customers are Land O Lakes, CHS and seven other regional cooperatives that wholesale the products to their members. Agriliance distributes agronomy products through approximately 2,200 local cooperatives from Ohio to the West Coast and from the Canadian border south to Kansas. Agriliance also provides sales and services through 48 Agriliance Service Centers and other retail outlets. Agriliance s

largest customer is the Company s Country Operations and Services business segment. In 2003, Agriliance sold approximately $1.3 billion of crop nutrient products and approximately $1.2 billion of crop protection and other products.

Industry; Competition

CF Industries. North American fertilizer producers operate in a highly competitive, global industry. Commercial fertilizers are world-traded commodities and producers compete principally on the basis of price and service. Many of the raw materials that are used in fertilizer production, such as natural gas, are often more expensive in the U.S. than other parts of the world. Crop nutrient margins and earnings have historically been cyclical; large profits generated throughout the mid-1990 s attracted additional capital and expansion and the industry now suffers from excess capacity. These factors have produced depressed margins for North American fertilizer manufacturers over the past several years, although recently fertilizer margins have stabilized.

CF Industries competes with numerous domestic and international crop nutrient manufacturers.

Agriliance. The wholesale distribution of agronomy products is highly competitive and dependent upon relationships with agricultural producers and local cooperatives, proximity to producers and local cooperatives and competitive pricing. Moreover, the crop protection products industry is mature with slow growth predicted for the future, which has led distributors and suppliers to turn to consolidation and strategic partnerships to benefit from economies of scale and increased market share. Agriliance competes with other large agronomy distributors, as well as other regional or local distributors and retailers. Agriliance competes on the strength of its relationships with the members of the Company, Farmland and Land O Lakes, its purchasing power and competitive pricing, and its attention to service in the field.

Major competitors of Agriliance in crop nutrient distribution include Agrium, Growmark, Cargill, United Suppliers and West Central. Major competitors of Agriliance in crop protection products distribution include Helena, ConAgra (UAP), Tenkoz and numerous smaller distribution companies.

Summary Operating Results

The Company accounts for its Agronomy business segment as follows:

CF Industries. The Company s investment in CF Industries of $153 million on August 31, 2003 is carried on the balance sheet at cost, including allocated patronage. Since CF Industries is a cooperative, the Company recognizes income from the investment only if it receives patronage refunds. Over the past five years CF Industries has realized operating losses and, as a result, it has not issued any patronage refunds to its members. Historically, crop nutrients manufacturing earnings have been cyclical in nature. CHS management has performed the appropriate impairment tests of this investment, and based upon those tests, believes that fair market value exceeds its carrying value. The Company will continue to perform impairment tests annually, including reviewing operating results, or as circumstances dictate, which could result in an impairment to its CF Industries investment.

Agriliance. At August 31, 2003 the Company s equity investment in Agriliance was $129.3 million. The Company recognizes earnings from Agriliance using the equity method of accounting, which results in the Company including its economic interest percentage of Agriliance s net earnings as equity income from investments. The Company applies related internal expenses against those earnings.

Summary operating results and identifiable assets for the Agronomy business segment for the fiscal years ended August 31, 2003, 2002 and 2001 are shown below:

	2003	2002	2001
		(dollars in thousands)	
Revenues:			
Net sales			
Patronage dividends	$ (84)	$ (89)	$ 196
Other revenues			
	(84)	(89)	196
Cost of goods sold			
Marketing, general and administrative	8,138	8,957	8,503
Operating losses	(8,222)	(9,046)	(8,307)
Interest	(974)	(1,403)	(4,529)
Equity income from investments	(20,773)	(13,425)	(7,360)
Income before income taxes	$ 13,525	$ 5,782	$ 3,582
Total identifiable assets August 31	$285,906	$242,015	$230,051

ENERGY

Overview

CHS is the nation s largest cooperative energy company based on sales, with operations that include petroleum refining and pipelines; the supply, marketing and distribution of refined fuels (gasoline, diesel, and other energy products); the blending, sale and distribution of lubricants; and the wholesale supply of propane. The Energy business segment processes crude oil into refined petroleum products at refineries in Laurel, Montana (wholly-owned) and McPherson, Kansas (an entity in which CHS has an approximately 74.5% ownership interest) and sells those products under the Cenex brand to CHS s member cooperatives and others, through a network of approximately 1,500 independent retailers, including approximately 800 that operate Cenex/ Ampride convenience stores.

Operations

Laurel Refinery. The Company s Laurel, Montana refinery processes medium and high sulfur crude oil into refined petroleum products that primarily include gasoline, diesel, and asphalt. The Laurel refinery sources approximately 90% of its crude oil supply from Canada, with the balance obtained from domestic sources. Laurel has access to Canadian and northwest Montana crude through the Company s wholly-owned Front Range Pipeline, LLC and other common carrier pipelines. The Laurel refinery also has access to Wyoming crude via common carrier pipelines from the south.

The Laurel facility processes approximately 55,000 barrels of crude oil per day to produce refined products that consist of approximately 42% gasoline, 30% diesel and other distillates and 28% asphalt and other residual products. Refined fuels produced at Laurel, Montana are available via the Yellowstone Pipeline to western Montana terminals and to Spokane and Moses Lake, Washington, south via common carrier pipelines to Wyoming terminals and Denver, Colorado, and east via the Company s wholly-owned Cenex Pipeline, LLC to Glendive, Montana, and Minot and Fargo, North Dakota.

McPherson Refinery. The McPherson, Kansas refinery is owned and operated by the National Cooperative Refinery Association (NCRA), of which the Company owns approximately 74.5%. The McPherson refinery processes low and medium sulfur crude oil into gasoline, diesel and other distillates,

propane, and other products. McPherson sources approximately 95% of its crude oil from Kansas, Oklahoma, and Texas through NCRA-owned and common carrier pipelines.

The McPherson refinery processes approximately 80,000 barrels of crude oil per day to produce refined products that consist of approximately 57% gasoline, 34% diesel and other distillates, and 9% propane and other products. Approximately 90% of the refined fuels are shipped via NCRA s proprietary products pipeline to its terminal in Council Bluffs, Iowa and to other markets via common carrier pipelines. The balance of the fuels are loaded into trucks at the refinery.

Other Energy Operations. The Company owns and operates three propane terminals, four asphalt terminals and three lubricants blending and packaging facilities. The Company also owns and leases a fleet of liquid and pressure trailers and tractors which are used to transport refined fuels, propane and anhydrous ammonia.

Products and Services

The Energy business segment produces and sells (primarily wholesale) gasoline, diesel, propane, asphalt, lubricants and other related products and provides transportation services. It obtains the petroleum products that it sells both from the Laurel and McPherson refineries and from third parties.

Sales and Marketing; Customers

The Company makes approximately 75% of its refined fuel sales to members, with the balance sold to non-members. Sales are made wholesale to member cooperatives and through a network of independent retailers that operate convenience stores under the Cenex/ Ampride tradename. The Company sold approximately 1.5 billion gallons of gasoline and approximately 1.3 billion gallons of diesel fuel in fiscal year 2003. The Company also wholesales auto and farm machinery lubricants to both members and non-members. In fiscal year 2003, energy operations sold approximately 23 million gallons of lube oil. The Company is one of the nation s largest propane wholesalers based on gallons sold. In fiscal year 2003, energy operations sold approximately 844 million gallons of propane. Most of the propane sold in rural areas is for heating and agricultural consumption. Annual sales volumes of propane vary greatly depending on weather patterns and crop conditions.

Industry; Competition

Governmental regulations and policies, particularly in the areas of taxation, energy and the environment, have a significant impact on the Company s Energy business segment. Like many other refineries, the Energy business segment s refineries are currently focusing their capital spending on reducing pollution. In particular, these refineries are currently working to comply with the Environmental Protection Agency low sulfur fuel regulations required by 2006, which are intended to lower the sulfur content of gasoline and diesel. The Company currently expects that the cost of compliance will be approximately $87.0 million for the Company s Laurel, Montana refinery and $324.0 million for NCRA s McPherson, Kansas refinery, of which $8.7 million had been spent at the Laurel refinery and $36.5 million had been spent by NCRA at the McPherson refinery as of August 31, 2003. The Company expects all of these compliance capital expenditures at the refineries to be complete by December 31, 2005, and anticipates funding these projects with a combination of cash flows from operations and debt proceeds.

The energy business is highly cyclical. Demand for crude oil and its products are driven by the condition of local and worldwide economies, local and regional weather patterns and taxation relative to other energy sources. Most of the Company s energy product market is located in rural areas, so sales activity tends to follow the planting and harvesting cycles. More fuel efficient equipment, reduced crop tillage, depressed prices for crops, warm winter weather, and government programs which encourage idle acres may all reduce demand for the Company s energy products.

The refining and wholesale fuels business is very competitive. Among the Company s competitors are some of the world s largest integrated petroleum companies, which have their own crude oil supplies,

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distribution and marketing systems. The Company also competes with smaller domestic refiners and marketers in the midwestern and northwestern United States, with foreign refiners who import products into the United States and with producers and marketers in other industries supplying other forms of energy and fuels to consumers. Given the commodity nature of the end products, profitability in the refining and marketing industry depends largely on margins, as well as operating efficiency, product mix, and costs of product distribution and transportation. The retail gasoline market is highly competitive, with much larger competitors that have greater brand recognition and distribution outlets throughout the country and the world. CHS owned and non-owned retail outlets are located primarily in the southern, midwestern and northwestern United States.

Summary Operating Results

Summary operating results and identifiable assets for the Energy business segment for the fiscal years ended August 31, 2003, 2002 and 2001 are shown below:

	2003	2002	2001
		(dollars in thousands)	
Revenues:			
Net sales	$3,648,093	$2,657,689	$2,781,243
Patronage dividends	415	458	712
Other revenues	10,461	6,392	4,036
	3,658,969	2,664,539	2,785,991
Cost of goods sold	3,475,947	2,489,352	2,549,099
Marketing, general and administrative	63,740	66,731	48,432
Operating earnings	119,282	108,456	188,460
Interest	16,401	16,875	25,097
Equity (income) loss from investments	(1,353)	1,166	4,081
Minority interests	20,782	14,604	34,713
Income before income taxes	$ 83,452	$ 75,811	$ 124,569
Total identifiable assets August 31	$1,449,652	$1,305,828	$1,154,036

COUNTRY OPERATIONS AND SERVICES

Overview

The Country Operations and Services business segment purchases a variety of grains from the Company s producer members and provides cooperative members and producers with access to a full range of products and services including farm supplies, programs for crop and livestock production, hedging and insurance services, and agricultural operations financing. Country Operations and Services operates at 282 locations dispersed throughout Minnesota, North Dakota, South Dakota, Nebraska, Montana, Idaho, Washington and Oregon. Most of these locations purchase grain from farmers and sell agronomy products, energy products and feed to those same producers and others, although not all locations provide every product and service.

Products and Services

Grain Purchasing. The Company is one of the largest country elevator operators in North America based on the number of country elevators. Through a majority of its elevator locations, the Country Operations and Services business segment purchases grain from member and non-member producers and other elevators and grain dealers. Most of the grain purchased is either sold through the Company s Grain Marketing business segment or used for local feed and processing operations. For the year ended August 31, 2003, the Country Operations and Services business segment purchased approximately

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298 million bushels of grain, primarily wheat (136 million bushels), corn (79 million bushels) and soybeans (46 million bushels). Of these bushels, 274 million were purchased from members and 204 million were sold through the Grain Marketing business segment.

Other Products. Country Operations and Services manufactures and sells other products, both directly and through ownership interests in other entities. These include seed; plant food; energy products; animal feed ingredients, supplements and products; animal health products; crop protection products; and processed sunflowers. The Company sells agronomy products at 155 locations, feed products at 128 locations and energy products at 93 locations. Farm supplies are purchased through cooperatives whenever possible.

Financial Services. The Company has provided open account financing to more than 150 CHS members that are cooperatives (cooperative association members) in the past year. These arrangements involve the discretionary extension of credit in the form of term and seasonal loans and can also be used as a clearing account for settlement of grain purchases and as a cash management tool. A substantial part of the term and seasonal loans are sold to the National Bank for Cooperatives (CoBank), with CoBank purchasing up to 90% of any loan. The Company s guarantee exposure on these loans at August 31, 2003 was approximately $6.7 million. Through its wholly-owned subsidiary Fin-Ag, Inc. the Company provides seasonal cattle feeding and swine financing loans, facility financing loans and crop production loans. It also provides consulting services to member cooperatives. Most loans are sold to CoBank under a separate program from that described above, under which the Company has guaranteed a portion of the loans. The Company s exposure at August 31, 2003 was approximately $43.0 million. The Company s borrowing arrangements allow for the Company to retain up to $110.0 million of loans in aggregate for both finance programs, or to sell the loans and extend guarantees up to $150.0 million in aggregate.

The Company s wholly-owned subsidiary Country Hedging, Inc., which is a registered futures commission merchant and a clearing member of both the Minneapolis Grain Exchange and the Kansas City Board of Trade, is a full service commodity futures and options broker.

Ag States Agency, LLC is an independent insurance agency in which the Company holds a majority ownership interest. It sells insurance, including group benefits, property and casualty, and bonding programs. Its approximately 1,600 customers are primarily agricultural businesses, including local cooperatives and independent elevators, oil stations, agronomy and feed/seed plants, implement dealers, fruit and vegetable packers/warehouses, and food processors.

Industry; Competition

Competitors for the purchase of grain include other elevators and large grain marketing companies. Competitors for farm supply include a variety of cooperatives, privately held and large national companies. The Company competes primarily on the basis of price, services and patronage.

Competitors to the Company s financing operations are primarily other financial institutions. The Company competes primarily on the basis of price, services and patronage. Country Hedging s competitors include international brokerage firms, national brokerage firms, regional brokerage firms (both cooperatives and non-cooperatives) as well as local introducing brokers, with competition driven by price and level of service. Ag States Agency, LLC competes with other insurance agencies, primarily on the basis of price and services.

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Summary Operating Results

Summary operating results and identifiable assets for the Country Operations and Services business segment for the fiscal years ended August 31, 2003, 2002 and 2001 are shown below:

	2003	2002	2001
		(dollars in thousands)	
Revenues:			
Net sales	$ 1,885,825	$ 1,474,553	$ 1,577,268
Patronage dividends	2,467	2,572	3,683
Other revenues	81,739	80,789	80,479
	1,970,031	1,557,914	1,661,430
Cost of goods sold	1,876,811	1,474,392	1,569,884
Marketing, general and administrative	55,887	47,995	53,417
Operating earnings	37,333	35,527	38,129
Gain on legal settlements	(10,867)	(2,970)	
Interest	14,975	13,851	15,695
Equity income from investments	(788)	(283)	(246)
Minority interests	1,168	786	385
Income before income taxes	$ 32,845	$ 24,143	$ 22,295
Total identifiable assets August 31	$ 857,523	$ 799,711	$ 679,053

GRAIN MARKETING

Overview

CHS is the nation s largest cooperative marketer of grain and oilseed based on grain storage capacity and grain sales, handling about 1.1 billion bushels annually. During fiscal year 2003, the Company purchased approximately 67% of total grain volumes from individual and member cooperatives and the Country Operations and Services business segment, with the balance purchased from third parties. CHS arranges for the transportation of the grains either directly to customers or to Company owned or leased grain terminals and elevators awaiting delivery to domestic and foreign purchasers. The Company primarily conducts its Grain Marketing operations directly, but does conduct some of its business through two 50% owned joint ventures.

Operations

The Grain Marketing segment purchases grain directly and indirectly from agricultural producers primarily in the midwestern and western United States. The purchased grain is typically contracted for sale for future delivery at a specified location, with the Company responsible for handling the grain and arranging for its transportation to that location. The sale of grain is recorded after title to the commodity has transferred and final weights, grades and settlement price have been agreed upon. Amounts billed to the customer as part of a sales transaction include the costs for shipping and handling. The Company s ability to arrange efficient transportation, including loading capabilities onto unit trains, ocean-going vessels, and barges, is a significant part of the service it offers to its customers. Rail, vessel, barge and truck transportation is carried out by third parties, often under long-term freight agreements with the Company. Grain intended for export is usually shipped by rail or barge to an export terminal, where it is loaded onto ocean-going vessels. Grain intended for domestic use is usually shipped by rail or truck to various locations throughout the country.

CHS owns export terminals, river terminals, and elevators involved in the handling and transport of grain. River terminals at St. Paul, Savage, and Winona, Minnesota, and Davenport, Iowa are used to load

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grains onto barges for shipment to both domestic and export customers via the Mississippi River System. The Company s export terminal at Superior, Wisconsin provides access to the Great Lakes and St. Lawrence Seaway, and an export terminal at Myrtle Grove, Louisiana serves the Gulf market. In the Pacific Northwest, the Company conducts its grain marketing operations through United Harvest, LLC (a 50% joint venture with United Grain Corporation) and TEMCO, LLC (a 50% joint venture with Cargill, Incorporated). United Harvest, LLC operates grain terminals in Vancouver and Kalama, Washington. TEMCO, LLC operates a large export terminal in Tacoma, Washington. These facilities serve the Pacific market, as well as domestic grain customers in the western United States. Grain Suppliers, LLC, a wholly-owned subsidiary (previously a 50% joint venture), operates elevator facilities in Friona, Texas and Collins, Mississippi. In 2003, the Company opened an office in Sao Paulo, Brazil for the procurement of soybeans for the Grain Marketing segment s international customers.

Grain Marketing purchases most of its grain during the summer and fall harvest period. Because of the Company s geographic location and the fact that it is further from its export facilities, grain tends to be sold later than in other parts of the country. However, as many producers have significant on-farm storage capacity and in light of the Company s own storage capacity, the Grain Marketing business segment buys and ships grain throughout the year. Due to the amount of grain purchased and held in inventory, the Grain Marketing business segment has significant working capital needs at various times of the year. The amount of borrowings for this purpose, and the interest rate charged on those borrowings, directly affect the profitability of the Grain Marketing segment.

Products and Services

The primary grains purchased by the Grain Marketing business segment for the year ended August 31, 2003 were corn (412 million bushels), wheat (329 million bushels) and soybeans (245 million bushels). Of the total grains purchased by the Grain Marketing business segment during the year ended August 31, 2003, 508 million bushels were purchased from the Company s individual and cooperative association members, 204 million bushels were purchased from the Country Operations and Services business segment and the remainder were purchased from third parties.

Sales and Marketing; Customers

Purchasers include domestic and foreign millers, maltsters, feeders, crushers, and other processors. To a much lesser extent purchasers include intermediaries and distributors. Grain Marketing operations are not dependent on any one customer. The Grain Marketing segment has supply relationships calling for delivery of grain at prevailing market prices.

Industry; Competition

The Grain Marketing business segment competes for both the purchase and sale of grain. Competition is intense and margins are low. Some competitors are integrated food producers, which may also be customers. A few major competitors have substantially greater financial resources than the Company.

In the purchase of grain from producers, location of the delivery facility is a prime consideration, but producers are increasingly willing to truck grain longer distances for sale. Price is affected by the capabilities of the facility; for example, if it is cheaper to deliver to a customer by unit train than by truck, a facility with unit train capability provides a price advantage. The Company believes that its relationships with individual members serviced by local Country Operations and Services locations and with cooperative members gives it a broad origination capability.

The Grain Marketing business segment competes for grain sales based on price, services and ability to provide the desired quantity and quality of grains. Location of facilities is a major factor in the ability to compete. Grain marketing operations compete with numerous grain merchandisers, including major grain merchandising companies such as Archer Daniels Midland (ADM), Cargill, Incorporated (Cargill), ConAgra, Bunge and Louis Dreyfus, each of which handle grain volumes of more than one billion bushels annually.

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The results of the grain marketing business may be adversely affected by relative levels of supply and demand, both domestic and international, commodity price levels (including grain prices reported on national markets) and transportation costs and conditions. Supply is affected by weather conditions, disease, insect damage, acreage planted and government regulations and policies. Demand may be affected by foreign governments and their programs, relationships of foreign countries with the United States, the affluence of foreign countries, acts of war, currency exchange fluctuations and substitution of commodities. Demand may also be affected by changes in eating habits, by population growth, and by increased or decreased per capita consumption of some products.

Summary Operating Results

Summary operating results and identifiable assets for the Grain Marketing business segment for the fiscal years ended August 31, 2003, 2002 and 2001 are shown below:

	2003	2002	2001
		(dollars in thousands)	
Revenues:			
Net sales	$4,139,226	$3,281,469	$3,416,239
Patronage dividends	218	497	840
Other revenues	25,458	21,902	22,964
	4,164,902	3,303,868	3,440,043
Cost of goods sold	4,133,677	3,272,985	3,416,500
Marketing, general and administrative	21,072	22,213	22,396
Operating earnings	10,153	8,670	1,147
Interest	4,738	4,807	8,144
Equity loss (income) from investments	1,673	(4,257)	(4,519)
Income (loss) before income taxes	$ 3,742	$ 8,120	$ (2,478)
Total identifiable assets August 31	$ 450,415	$ 481,232	$ 345,696

PROCESSED GRAINS AND FOODS

Overview

The Processed Grains and Foods business segment converts raw agricultural commodities into ingredients for finished food products or into finished consumer food products. The Company has focused on areas that allow it to utilize the products supplied by member producers. These areas are oilseed processing, wheat milling and foods.

Oilseed Processing

The Company s oilseed processing operations convert soybeans into soybean meal, soyflour, crude soyoil, refined soybean oil and associated by-products. These operations are conducted at a facility in Mankato, Minnesota that can crush 39 million bushels of soybeans on an annual basis, producing approximately 940,000 short tons of soybean meal and 460 million pounds of crude soybean oil. The same facility is able to produce approximately 1 billion pounds of refined soybean oil annually. Another crushing facility in Fairmont, Minnesota has a crushing capacity and crude soyoil output similar to the Mankato facility. The facility in Fairmont was essentially complete and became operational in the first fiscal quarter of 2004. Total costs for this new facility are estimated to be approximately $85.0 million, of which $68.9 million has been spent through August 31, 2003.

The Company s oilseed processing operations produce three primary products: refined oils, soybean meal and soyflour. Refined oils are used in processed foods, such as margarine, shortening, salad dressings

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and baked goods and, to a lesser extent for certain industrial uses for plastics, inks and paints. Soybean meal has a high protein content and is used for feeding livestock. Soyflour is used in the baking industry, as a milk replacement in animal feed and in industrial applications.

The Company s soy processing facilities are located in areas with a strong production base of soybeans and end-user market for the meal and soyflour. The Company purchases virtually all of its soybeans from members. The oilseed crushing operations currently produce approximately 45% of the crude oil that the Company refines; it purchases the balance from outside suppliers. Once the Fairmount, Minnesota crushing facility is fully operational, the oilseed crushing operations will produce approximately 85% of the crude oil the Company refines.

The Company s customers for refined oil are principally large food product companies located throughout the United States. However, over 50% of the customers are located in the midwest due to lower freight costs and slightly higher profitability. The largest customer for refined oil products is Ventura Foods, LLC (Ventura Foods), in which the Company holds a 50% ownership interest and with which the Company has a long-term supply agreement to supply minimum quantities of edible soybean oils as long as the Company maintains a minimum 25.5% ownership interest and the Company s price is comparative with other suppliers of the product. The Company s sales to Ventura Foods were $78.5 million in fiscal year 2003. The Company also sells soymeal to almost 400 customers, primarily feed lots and feed mills in southern Minnesota; five of these customers accounted for approximately 58% of the soymeal sold. One customer accounted for 25% of soymeal sold and another customer accounted for 12% of soymeal sold. The Company sells soyflour to customers in the baking industry both domestically and for export.

The refined soybean products industry is highly competitive. Major industry competitors include ADM, Cargill, Ag Processing, Inc., and Bunge. These and other competitors have acquired other processors and have expanded existing plants, or are proposing to construct new plants, both domestically and internationally. Price, transportation costs, services and product quality drive competition. The Company estimates that it has a market share of approximately 4% to 5% of the domestic refined soybean oil market and less than 3% of the domestic soybean crushing capacity.

Soybeans are a commodity and their price can fluctuate significantly depending on production levels, demand for the refined products, and other supply and demand factors.

Wheat Milling

In January 2002, the Company and Cargill formed Horizon Milling, LLC (Horizon Milling), in which the Company owns 24% and Cargill owns the remaining 76%. Horizon Milling is the largest U.S. wheat miller based on milling capacity. Sales and purchases of wheat and durum by the Company to Horizon Milling during fiscal year 2003 were $191.3 million and $8.8 million, respectively. Horizon Milling s advance payments on grain to the Company were $7.5 million on August 31, 2003, and are included in Customer advance payments on the Company s Consolidated Balance Sheets.

The Company ceased operations at its Huron, Ohio mill prior to the formation of Horizon Milling and the Company s facility lease expired on September 30, 2002. The Company has dismantled the milling equipment and is currently negotiating for the sale of the equipment that has not yet been sold. The Processed Grains and Foods business segment established an impairment of approximately $6.5 million on the equipment during the fourth quarter of fiscal year 2002.

Foods

The Company has two primary areas of focus in the foods area: Ventura Foods, which produces oilseed based products such as margarine and salad dressing and which is 50% owned by the Company, and the production of Mexican foods such as tortillas, tortilla chips and entrees.

Ventura Foods. Ventura Foods manufactures, packages, distributes and markets bulk margarine, salad dressings, mayonnaise, salad oils, syrups, soup bases and sauces, many of which utilize soybean oil as a primary ingredient. Approximately 30% of Ventura Food s volume, based on sales revenues, comes from

products for which Ventura Foods owns the brand, and the remainder comes from products that it produces for third parties. A variety of Ventura Food s product formulations and processes are proprietary to it or its customers. Ventura Foods is one of the largest manufacturers of margarine in the U.S. based on sales and is a major producer of many other products.

Ventura Foods has 13 manufacturing and distribution locations across the United States. It sources its raw materials, which consists primarily of soybean oil, canola oil, cottonseed oil, peanut oil and various other ingredients and supplies, from various national suppliers, including the Company s oilseed processing operations. It sells the products it manufactures to third parties as a contract manufacturer, as well as directly to retailers, food distribution companies and large institutional food service companies. Ventura Foods sales are approximately 60% in foodservice and the remainder split between retail and industrial customers who use edible oil products as ingredients in foods they manufacture for resale. One customer accounted for 23% of net sales during Ventura Foods 2003 fiscal year.

Ventura Foods competes with a variety of large companies in the food manufacturing industry. Some of its major competitors are ADM, Cargill, Bunge, Unilever, ConAgra, ACH, Smuckers, Kraft, and CF Sauer.

Ventura Foods was created in 1996 and at the time was owned 40% by the Company and 60% by Wilsey Foods, Inc., a majority owned subsidiary of Mitsui & Co., Ltd. In March 2000, the Company purchased an additional 10% interest from Wilsey Foods, Inc. bringing the Company s total equity investment in Ventura Foods to 50%. The Company accounts for the Ventura Foods investment under the equity method of accounting.

Mexican Foods. Since June 2000, the Company has acquired three regional producers of Mexican foods. Through its Mexican foods operations, the Company manufactures, packages, and distributes tortillas, tortilla chips and prepared frozen Mexican food products such as burritos and tamales. The Company sells these products under a variety of local and regional brand names and also produces private label products and co-packs for customers. The current operational focus is on integrating these disparate operations into a single business entity with consistent standards, systems and sales practices.

The tortilla and tortilla chip industry in the United States is comprised of a large number of small regional manufacturers and a few dominant manufacturers. The Company estimates that its Mexican foods operation has approximately a 1.5% share of the national tortilla market and less than a 1% share of the national tortilla chip market. On a national basis, the primary competitors are large chip and snack companies such as Frito Lay. During the Company s fiscal year ended August 31, 2003 one customer accounted for 13% of Mexican foods net sales and another customer accounted for 12% of net sales.

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Summary Operating Results

Summary operating results and identifiable assets for the Processed Grains and Foods business segment for the fiscal years ended August 31, 2003, 2002 and 2001 are shown below:

	2003	2002	2001
		(dollars in thousands)	
Revenues:			
Net sales*	$491,931	$496,084	$662,726
Patronage dividends	111	260	339
Other revenues	2,300	(1,469)	(238)
	494,342	494,875	662,827
Cost of goods sold	466,857	457,538	619,184
Marketing, general and administrative	36,540	36,930	44,870
Operating (losses) earnings	(9,055)	407	(1,227)
Interest	12,845	9,514	13,026
Equity income from investments	(26,056)	(41,331)	(35,505)
Income before income taxes	$ 4,156	$ 32,224	$ 21,252
Total identifiable assets August 31	$498,872	$439,942	$430,871

* The sales decline from 2001 is primarily due to the formation of Horizon Milling. Since January 2002 the Company has accounted for the operating results of its milling operations under the equity method of accounting. Earnings from the Company s interest in Horizon Milling are included as part of equity income from investments.

PRICE RISK AND HEDGING

Whenever the Company enters into a commodity purchase commitment it incurs risks of carrying inventory, including risks related to price changes and performance (including delivery, quality, quantity and shipment period). The Company is exposed to risk of loss in the market value of positions held, consisting of inventory and purchase contracts at a fixed or partially fixed price in the event market prices decrease. The Company is also exposed to risk of loss on its fixed price or partially fixed price sales contracts in the event market prices increase.

To reduce the price change risks associated with holding fixed price commitments, the Company generally takes opposite and offsetting positions by entering into commodity futures contracts (either a straight futures contract or an options futures contract) on regulated commodity futures exchanges for grain, and regulated mercantile exchanges for refined products and crude oil. The crude oil and most of the grain and oilseed volume handled by the Company can be hedged. Some grains cannot be hedged because there are no futures for certain commodities. For those commodities, risk is managed through the use of forward sales and various pricing arrangements and to some extent cross-commodity futures hedging. While hedging activities reduce the risk of loss from changing market values of inventory, such activities also limit the gain potential which otherwise could result from changes in market prices of inventory. The Company s policy is to generally maintain hedged positions in grain. The Company s profitability from operations is primarily derived from margins on products sold and grain merchandised, not from hedging transactions. Hedging arrangements do not protect against nonperformance of a contract.

When a futures contract is entered into, an initial margin deposit must be sent to the applicable exchange or broker. The amount of the deposit is set by the exchange and varies by commodity. If the market price of a short futures contract increases, then an additional margin deposit (maintenance margin) would be required. Similarly, if the price of a long futures contract decreases, a maintenance margin

deposit would be required and sent to the applicable exchange. Subsequent price changes could require additional maintenance margins or could result in the return of maintenance margins.

At any one time, inventory and purchase contracts for delivery to the Company may be substantial. The Company has risk management policies and procedures that include net position limits. These limits are defined for each commodity and include both trader and management limits. This policy, and computerized procedures in grain marketing operations, requires a review by operations management when any trader is outside of position limits and also a review by senior management of the Company if operating areas are outside of position limits. A similar process is used in energy operations. The position limits are reviewed at least annually with the management of the Company. The Company monitors current market conditions and may expand or reduce its risk management policies or procedures in response to changes in those conditions. In addition, all purchase and sale contracts are subject to credit approvals and appropriate terms and conditions.

EMPLOYEES

At August 31, 2003, CHS had approximately 6,820 full and part-time employees, which included approximately 560 employees of NCRA. Of that total, approximately 1,890 were employed in the Energy segment, 2,440 in the Country Operations and Services segment (not including an estimated 1,010 seasonal and temporary employees), 440 in the Grain Marketing segment, 850 in the Processed Grains and Foods segment and 190 in corporate and administrative functions. In addition to those employed directly by the Company, many employees work for the joint ventures in which the Company has an ownership interest. All of the employees in the Agronomy segment and a portion of the Grain Marketing and Processed Grains and Foods segments are employed in this manner.

Employees in certain areas are represented by collective bargaining agreements. Refinery workers in Laurel, Montana (185 employees), are represented by agreements with two unions (Paper, Allied-Industrial, Chemical and Energy Workers International Union (PACE) and Oil Basin Pipeliners Union (OBP)), for which agreements are in place through 2006 for PACE, and through 2006 for OBP in regard to wages and benefits. The contracts covering the NCRA McPherson, Kansas refinery (254 employees in the PACE union) are also in place through 2006. There are approximately 170 employees in transportation and lubricant plant operations that are covered by collective bargaining agreements that expire at various times. Production workers in grain marketing operations (144 employees) are represented by agreements with four unions which expire at various times from 2003 through 2005. In particular, grain marketing employees in the Bakers, Confectionary, Tobacco Workers and Grain Millers International Union in Superior, Wisconsin (49 employees) have contracts that have expired and are currently being negotiated, with the Company anticipating a successful resolution. Finally, certain production workers in oilseed processing operations are subject to collective bargaining agreements with the American Federation of Grain Millers (127 employees) and the Pipefitters Union (2 employees) for which agreements are in place through 2006.

MEMBERSHIP IN THE COMPANY AND AUTHORIZED CAPITAL

Introduction

The Company is an agricultural membership cooperative organized under Minnesota cooperative law to do business with member and non-member patrons. Patrons, and not the Company, are subject to income taxes on income from patronage. The Company is subject to income taxes on non-patronage-sourced income. See Tax Treatment below.

Distribution of Net Income; Patronage Refunds

The Company is required by its organizational documents annually to distribute net earnings derived from patronage business with members, after payment of dividends on equity capital, to members on the basis of patronage, except that the Board of Directors may elect to retain and add to the Company s

unallocated capital reserve an amount not to exceed 10% of the distributable net income from patronage business. Net income from non-patronage business may be distributed to members or added to the unallocated capital reserve, in whatever proportions the Board of Directors deems appropriate.

These distributions, referred to as patronage refunds or patronage dividends, may be distributed in cash, patrons equities, revolving fund certificates, securities of the Company or others or any combination designated by the Board of Directors. Since 1998, the Board of Directors has distributed patronage refunds the form of 30% cash and 70% patrons equities (see Patrons Equities below). The Board of Directors may change the mix in the form of the patronage refunds in the future. In making distributions, the Board of Directors may use any method of allocation that, in its judgment, is reasonable and equitable. Patronage refunds distributed during the years ended August 31, 2003, 2002 and 2001 were $88.3 million ($26.5 million in cash), $132.6 million ($40.1 million in cash) and $86.4 million ($26.1 million in cash), respectively.

Patrons Equities

Patrons equities are in the form of a book entry and represent a right to receive cash or other property, including securities, when redeemed by the Company. Patrons equities form part of the capital of the Company, do not bear interest and are not subject to redemption upon request of a member. Patrons equities are redeemable only at the discretion of the Board of Directors and in accordance with the terms of the redemption policy adopted by the Board of Directors, which may be modified at any time without member consent. The Company s bylaws grant the Board of Directors the discretion to redeem patrons equities upon such terms as the Board of Directors may, from time to time, determine. The Company s current policy is to redeem the equities of those members who were age 61 and older on June 1, 1998 when they reach the age of 72 and upon death. The current policy also provides for an annual pro-rata redemption of equities older than 10 years held by active members in an amount determined by the Board of Directors.

Redemptions of patrons and other equities, including equity participation units (discussed in Note 9 to the Consolidated Financial Statements), during the years ended August 31, 2003, 2002 and 2001 were $31.1 million, $31.1 million and $33.0 million, respectively.

Governance

The Company is managed by a Board of Directors of at least 17 persons elected by the members at the Company s annual meeting. Terms of Directors are staggered so that no more than seven directors are elected in any year. The Board of Directors is currently comprised of 17 directors. The articles of incorporation and bylaws of the Company may be amended only upon approval of a majority of the votes cast at an annual or special meeting of the members, except for the higher vote described under Certain Antitakeover Measures below.

Membership

Membership in the Company is restricted to certain producers of agricultural products and to associations of producers of agricultural products that are organized and operating so as to adhere to the provisions of the Agricultural Marketing Act and the Capper-Volstead Act, as amended. The Board of Directors may establish other qualifications for membership as it may from time to time deem advisable.

As a membership cooperative, the Company does not have common stock. The Company may issue equity or debt securities, on a patronage basis or otherwise, to its members. The Company has two classes of outstanding membership. Individual members are individuals actually engaged in the production of agricultural products. Cooperative associations are associations of agricultural producers, either cooperatives or other associations organized and operated under the provisions of the Agricultural Marketing Act and the Capper-Volstead Act.

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Voting Rights

Voting rights arise by virtue of membership in the Company, not because of ownership of any equity or debt security. Members that are cooperative associations are entitled to vote based upon a formula that takes into account the equity held by the cooperative in the Company and the average amount of business done with the Company over the previous three years.

Members who are individuals are entitled to one vote. Individual members may exercise their voting power directly or through a patrons association associated with a grain elevator, feed mill, seed plant or any other Company facility (with certain historical exceptions) recognized by the Board of Directors. The number of votes of patrons associations is determined under the same formula as cooperative association members.

Most matters submitted to a vote of the members require the approval of a majority of the votes cast at a meeting of the members, although the approval of not less than two-thirds of the votes cast at a meeting is required to approve Change of Control transactions, which include a merger, consolidation, liquidation, dissolution, or the sale of all or substantially all of the Company s assets and, in certain circumstances, a greater vote may be required. See Certain Antitakeover Measures below.

Debt and Equity Instruments

The Company may issue debt and equity instruments to its current members and patrons, on a patronage basis or otherwise, and to persons who are neither members nor patrons. Under our articles of incorporation, equity issued by the Company is subject to a first lien in favor of the Company for all indebtedness of the holder to the Company. As of August 31, 2003, the Company s outstanding capital included patrons equities (consisting of capital equity certificates and non-patronage earnings certificates), 8% Cumulative Redeemable Preferred Stock (dividends paid quarterly) and certain capital reserves.

Distribution of Assets Upon Dissolution; Merger and Consolidation

In the event of any dissolution, liquidation or winding up of the Company, whether voluntary or involuntary, all debts and liabilities would be paid first according to their respective priorities. As more particularly provided in the Company s bylaws, the remaining assets would be paid to the holders of equity capital to the extent of their interests and any excess would be paid to patrons on the basis of their past patronage. The bylaws provide for the allocation among the members and nonmember patrons of the consideration received in any merger or consolidation to which the Company is a party.

Certain Antitakeover Measures

The Company s governing documents may be amended upon the approval of a majority of the votes cast at an annual or special meeting. However, if the Board of Directors, in its sole discretion, declares that a proposed amendment to the Company s governing documents involves or is related to a hostile takeover, the amendment must be adopted by 80% of the total voting power of the members of the Company. Further, if the Board of Directors determines that a proposed change of control transaction involves a hostile takeover, the 80% approval requirement applies. The term hostile takeover is not further defined in the Minnesota cooperative law or the governing documents of the Company.

Tax Treatment

Subchapter T of the Internal Revenue Code sets forth rules for the tax treatment of cooperatives and applies to both cooperatives exempt from taxation under Section 521 of the Internal Revenue Code and to nonexempt corporations operating on a cooperative basis. The Company is a nonexempt cooperative.

As a cooperative, the Company is not taxed on patronage paid to its members either in the form of equities or cash. Consequently, such amounts are taxed only at the patron level. However, the amounts of any allocated but undistributed patronage earnings (called non-qualified unit retains) are taxable to the

Company when allocated. Upon redemption of any such non-qualified unit retains, the amount is deductible to the Company and taxable to the member.

Income derived by the Company from non-patronage sources is not entitled to the single tax benefit of Subchapter T and is taxed to the Company at corporate income tax rates.

NCRA is not consolidated for tax purposes.

Item 2. ***Properties***

The Company owns or leases energy, grain handling and processing, food manufacturing and agronomy related facilities throughout the United States. Below is a summary of these locations.

Energy

Facilities in the Company s Energy business segment include the following, all of which are owned except where indicated as leased:

Refinery	Laurel, Montana
Propane terminals	3 locations in Minnesota, North Dakota and Wisconsin
Transportation terminals/repair facilities	10 locations in Iowa, Minnesota, Montana, North Dakota, South Dakota, Washington and Wisconsin, 2 of which are leased
Petroleum & asphalt terminals/storage facilities	9 locations in Montana, North Dakota and Wisconsin
Pump stations	10 locations in Montana and North Dakota
Pipelines:	
Cenex Pipeline, LLC	Laurel, Montana to Fargo, North Dakota
Front Range Pipeline, LLC	Canadian Border to Laurel, Montana
Convenience stores/gas stations	33 locations in Iowa, Minnesota, Montana, South Dakota and Wyoming
Lubricant plants/warehouses	3 locations in Minnesota, Ohio and Texas

The Company has a 74.5% interest in NCRA, which owns and operates the following facilities:

Refinery	McPherson, Kansas
Petroleum terminals/storage	2 locations in Iowa and Kansas
Pipeline	McPherson, Kansas to Council Bluffs, Iowa
Jayhawk Pipeline	Throughout Kansas, with branches in Oklahoma and Texas
Jayhawk stations	40 locations located in Kansas and Oklahoma

Grain Marketing

The Company owns or leases grain terminals used in the Grain Marketing business segment at the following locations:

Davenport, Iowa (2 owned terminals)
Kalama, Washington (leased)
Kansas City, Missouri (leased)
Minneapolis, Minnesota (owned idle terminal)
Myrtle Grove, Louisiana (owned)
St. Paul, Minnesota (leased)
Savage, Minnesota (owned)
Spokane, Washington (owned)
Superior, Wisconsin (owned)
Winona, Minnesota (1 owned, 1 leased)

Country Operations and Services

In the Country Operations and Services business segment the Company owns 282 agri operations locations (of which some of the facilities are on leased land), 8 feed manufacturing facilities and 2 sunflower plants located in Minnesota, Nebraska, North Dakota, South Dakota, Montana, Washington, Oregon and Idaho.

Processed Grains and Foods

Within the Processed Grains and Foods business segment, the Company owns and leases the following facilities:

Oilseed Processing

The Company owns a campus in Mankato, Minnesota, comprised of a crushing plant, an oilseed refinery, a soyflour plant and a quality control laboratory. A crushing plant in Fairmont, Minnesota previously under construction was essentially complete and became operational during the fiscal quarter ending November 30, 2003.

Wheat Milling

The Company owns five flour milling facilities at the following locations that are leased to Horizon Milling, LLC:

Rush City, Minnesota
Kenosha, Wisconsin
Houston, Texas
Mount Pocono, Pennsylvania
Fairmount, North Dakota

Foods

The Company leases manufacturing facilities in New Brighton, Minnesota, Ft. Worth, Texas and Phoenix, Arizona. In addition, the Company owns two manufacturing facilities in Ft. Worth, Texas. A new facility is currently under construction near Newton, North Carolina, which the Company expects to complete during its fiscal quarter ending November 30, 2003. The Company originally intended to use the facility for manufacturing upon completion of construction, but at this time the Company expects to sell or lease it. All facilities are related to the Company s Mexican foods operations.

Corporate Headquarters

The Company is headquartered in Inver Grove Heights, Minnesota. The Company owns a 33-acre campus consisting of one main building with approximately 320,000 square feet of office space and two smaller buildings with approximately 13,400 and 9,000 square feet of space.

The Company s internet address is www.chsinc.com.

Item 3. ***Legal Proceedings***

The Company is involved as a defendant in various lawsuits, claims and disputes which are in the normal course of the Company s business. The resolution of any such matters may affect consolidated net income for any fiscal period; however, management believes any resulting liabilities, individually or in the aggregate, will not have a material effect on the consolidated financial position, results of operations or cash flows of the Company during any fiscal year.

In October 2003, the Company and NCRA reached agreement with the Environmental Protection Agency (EPA) and the State of Montana s Department of Environmental Quality and the State of Kansas Department of Health and Environment, respectively, regarding the terms of settlements with respect to

reducing air emissions at the Company s Laurel, Montana and NCRA s McPherson, Kansas refineries. These settlements are part of a series of similar settlements that the EPA has negotiated with major refiners under the EPA s Petroleum Refinery Initiative. The settlements, which resulted from nearly three years of discussions, take the form of consent decrees filed with the U.S. District Court for the District of Montana (Billings Division) and the U.S. District Court for the District of Kansas, respectively. Each consent decree details specific capital improvements, supplemental environmental projects and operational changes that the Company and NCRA have agreed to implement at the relevant refinery over the next several years. The consent decrees also require the Company and NCRA to pay approximately $0.5 million in aggregate civil cash penalties. The Company and NCRA anticipate that their aggregate capital expenditures related to these settlements will total approximately $25.0 million to $30.0 million over the next eight years. Approximately 50 percent of the expenditures will be made over the first three years. The Company does not believe that the settlements will have a material adverse affect on the Company.

Item 4. ***Submission of Matters to a Vote of Security Holders***

The Company held a special meeting on August 5, 2003 where results of a mail ballot were counted to change the Company s legal name to CHS Inc. Fifty percent of CHS members, consisting of cooperatives and producers in 27 states, participated in the vote; of these, eighty-seven percent of members voted in favor of the legal name change, which needed a simple majority of the members voting for passage.

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PART II.

Item 5. ***Market for Registrant s Common Equity and Related Stockholder Matters***

The Company has approximately 51,100 members, of which approximately 1,100 are cooperative association members and approximately 50,000 are individual members. As a cooperative, the Company does not have any common equity that is traded.

On August 31, 2003 the Company had 3,748,099 shares of 8% Cumulative Redeemable Preferred Stock outstanding, which is listed on the NASDAQ National Market under the symbol CHSCP.

The Company sold no equity securities during the three years ended August 31, 2003 that were not registered under the Securities Act of 1933, as amended.

On April 25, 2003, the Company issued 298,099 shares of its 8% Cumulative Redeemable Preferred Stock (the New Shares) on conversion of 7,452,439 then-outstanding shares of 8% Preferred Stock (the Old Shares). The New Shares were exchanged by the Company with its existing security holders (the holders of the Old Shares) exclusively and no commission or other remuneration was paid or given directly or indirectly for soliciting the exchange. Accordingly, the Company relied on the exemption from registration contained in Section 3(a)(9) of the Securities Act of 1933, as amended, for the issuance of the New Shares and did not file a registration statement with the Securities and Exchanges Commission with respect to that issuance.

Item 6. ***Selected Financial Data***

The selected financial information below has been derived from the Company s consolidated financial statements for the years ended August 31. The selected consolidated financial information for August 31, 2003, 2002 and 2001 should be read in conjunction with the Company s consolidated financial statements and notes thereto included elsewhere in this filing.

Summary Consolidated Financial Data

	2003	2002	2001	2000	1999
			(dollars in thousands)		
Income Statement Data:					
Revenues:					
Net sales	$9,270,734	$7,156,454	$7,464,242	$8,248,413	$6,198,843
Patronage dividends	3,257	3,885	5,977	5,494	5,876
Other revenues	124,542	109,459	116,254	97,471	81,180
	9,398,533	7,269,798	7,586,473	8,351,378	6,285,899
Cost of goods sold	9,058,951	6,940,926	7,181,433	8,051,057	6,010,796
Marketing, general and administrative	190,582	187,292	184,046	155,266	152,031
Operating earnings	149,000	141,580	220,994	145,055	123,072
Gain on legal settlements	(10,867)	(2,970)			
Interest	48,675	42,455	61,436	57,566	42,438
Equity income from investments	(47,299)	(58,133)	(28,494)	(28,325)	(22,363)
Minority interests	21,950	15,390	35,098	24,546	10,017
Income before income taxes	136,541	144,838	152,954	91,268	92,980
Income taxes	12,700	18,700	(25,600)	3,880	6,980
Net income	$ 123,841	$ 126,138	$ 178,554	$ 87,388	$ 86,000

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	2003	2002	2001	2000	1999
	(dollars in thousands)				
Balance Sheet Data (at August 31):					
Working capital	$ 458,738	$ 249,115	$ 305,280	$ 214,223	$ 219,045
Net property, plant and equipment	1,122,982	1,057,421	1,023,872	1,034,768	968,333
Total assets	3,807,968	3,481,727	3,057,319	3,172,680	2,787,664
Long-term debt, including current maturities	663,173	572,124	559,997	510,500	482,666
Total equities	1,481,711	1,289,638	1,261,153	1,164,426	1,117,636

The selected financial statement information below has been derived from the Company s five business segments, and Corporate and Other, for the fiscal years ended August 31, 2003, 2002 and 2001. The intercompany sales between segments were $894.3 million, $753.3 million and $973.2 million for the fiscal years ended August 31, 2003, 2002 and 2001, respectively.

Summary Financial Data By Business Segment

	Agronomy			Energy		
	2003	2002	2001	2003	2002	2001
	(dollars in thousands)					
Revenues:						
Net sales				$3,648,093	$2,657,689	$2,781,243
Patronage dividends	$ (84)	$ (89)	$ 196	415	458	712
Other revenues				10,461	6,392	4,036
	(84)	(89)	196	3,658,969	2,664,539	2,785,991
Cost of goods sold				3,475,947	2,489,352	2,549,099
Marketing, general and administrative	8,138	8,957	8,503	63,740	66,731	48,432
Operating (losses) earnings	(8,222)	(9,046)	(8,307)	119,282	108,456	188,460
Interest	(974)	(1,403)	(4,529)	16,401	16,875	25,097
Equity (income) loss from investments	(20,773)	(13,425)	(7,360)	(1,353)	1,166	4,081
Minority interests				20,782	14,604	34,713
Income before income taxes	$ 13,525	$ 5,782	$ 3,582	$ 83,452	$ 75,811	$ 124,569
Total identifiable assets August 31	$285,906	$242,015	$230,051	$1,449,652	$1,305,828	$1,154,036

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	Country Operations and Services			Grain Marketing		
	2003	2002	2001	2003	2002	2001
	(dollars in thousands)					
Revenues:						
Net sales	$1,885,825	$1,474,553	$1,577,268	$4,139,226	$3,281,469	$3,416,239
Patronage dividends	2,467	2,572	3,683	218	497	840
Other revenues	81,739	80,789	80,479	25,458	21,902	22,964
	1,970,031	1,557,914	1,661,430	4,164,902	3,303,868	3,440,043
Cost of goods sold	1,876,811	1,474,392	1,569,884	4,133,677	3,272,985	3,416,500
Marketing, general and administrative	55,887	47,995	53,417	21,072	22,213	22,396
Operating earnings	37,333	35,527	38,129	10,153	8,670	1,147
Gain on legal settlements	(10,867)	(2,970)				
Interest	14,975	13,851	15,695	4,738	4,807	8,144
Equity income (loss) from investments	(788)	(283)	(246)	1,673	(4,257)	(4,519)
Minority interests	1,168	786	385			
Income (loss) before income taxes	$ 32,845	$ 24,143	$ 22,295	$ 3,742	$ 8,120	$ (2,478)
Total identifiable assets August 31	$ 857,523	$ 799,711	$ 679,053	$ 450,415	$ 481,232	$ 345,696

	Processed Grains and Foods			Corporate and Other		
	2003	2002	2001	2003	2002	2001
	(dollars in thousands)					
Revenues:						
Net sales	$491,931	$496,084	$662,726			
Patronage dividends	111	260	339	$ 130	$ 187	$ 207
Other revenues	2,300	(1,469)	(238)	4,584	1,845	9,013
	494,342	494,875	662,827	4,714	2,032	9,220
Cost of goods sold	466,857	457,538	619,184			
Marketing, general and administrative	36,540	36,930	44,870	5,205	4,466	6,428
Operating (losses) earnings	(9,055)	407	(1,227)	(491)	(2,434)	2,792
Interest	12,845	9,514	13,026	690	(1,189)	4,003
Equity (income) loss from investments	(26,056)	(41,331)	(35,505)	(2)	(3)	15,055
Income (loss) before income taxes	$ 4,156	$ 32,224	$ 21,252	$ (1,179)	$ (1,242)	$ (16,266)
Total identifiable assets August 31	$498,872	$439,942	$430,871	$265,600	$212,999	$217,612

Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

CHS Inc. (CHS or the Company) is one of the nation s leading integrated agricultural companies. As a cooperative, the Company is owned by farmers, ranchers and their local cooperatives from the Great Lakes to the Pacific Northwest and from the Canadian border to Texas. CHS buys commodities from, and provides products and services to members and other customers. The Company provides a wide variety of products and services, from initial agricultural inputs such as fuels, farm supplies and crop nutrients, to agricultural outputs that include grains and oilseeds, grain and oilseed processing, and food products.

The Company has five distinct business segments: Agronomy, Energy, Country Operations and Services, Grain Marketing and Processed Grains and Foods. Summary data for each of these segments for the fiscal years ended August 31, 2003, 2002 and 2001 is shown on prior pages.

Many of the Company s business activities are highly seasonal, and as a result, operating results will vary throughout the year. Overall, the Company s income is generally lowest during the second fiscal

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quarter and highest during the third fiscal quarter. Certain business segments are subject to varying seasonal fluctuations. For example, the Agronomy and Country Operations and Services segments experience higher volumes and income during the spring planting season and in the fall, which corresponds to harvest. The Grain Marketing segment is subject to fluctuations in volume and earnings based on producer harvests, world grain prices and demand. The Company s Energy segment generally experiences higher volumes and profitability in certain operating areas, such as refined products, in the summer when gasoline and diesel usage is highest. Other energy products, such as propane, experience higher volumes and profitability during the winter heating and crop drying seasons.

The Company s revenue can be significantly affected by global market prices for commodities such as petroleum products, natural gas, grain, oilseeds and flour. Changes in market prices for commodities that the Company purchases without a corresponding change in the selling prices of those products can affect revenues and operating earnings. Commodity prices are affected by a wide range of factors beyond the Company s control, including the weather, crop damage due to disease or insects, drought, the availability and adequacy of supply, government regulation and policies, world events, and general political and economic conditions.

While the Company s sales and operating results are derived from businesses and operations which are wholly-owned and majority-owned, a portion of business operations are conducted through companies in which the Company holds ownership interests of 50% or less and does not control the operations. The Company accounts for these investments primarily using the equity method of accounting, wherein CHS records as equity income from investments its proportionate share of income or loss reported by the entity, without consolidating the revenues and expenses of the entity in the Company s consolidated statements of operations. These investments principally include the Company s 25% ownership in Agriliance, LLC (Agriliance), the 50% ownership in TEMCO, LLC, the 50% ownership in United Harvest, LLC, the 24% ownership in Horizon Milling, LLC (Horizon) and the 50% ownership in Ventura Foods, LLC (Ventura).

Agriliance is owned and governed by Land O Lakes, Inc. (50%) and United Country Brands, LLC (50%). United Country Brands, LLC is owned and governed 50% by the Company and 50% by Farmland Industries, Inc. (Farmland), and was formed solely to hold a 50% interest in Agriliance. Prior to the transaction described below, the Company s indirect share of earnings (economic interest) in Agriliance was 25%, which was the same as the Company s ownership or governance interest. Subsequent to the transaction, the Company s indirect economic interest in Agriliance is no longer the same as the Company s ownership or governance interest.

In April 2003, the Company acquired an additional economic interest in the Agriliance wholesale crop protection business (the CPP Business), which constitutes only a part of the Agriliance business operations. The Company acquired 13.1% of the CPP Business for a cash payment of $34.3 million. The economic interests in Agriliance are owned 50% by Land O Lakes, 25% plus an additional 13.1% of the CPP Business by the Company and 25% less 13.1% of the CPP Business by Farmland. The ownership or governance interests in Agriliance did not change with the purchase of this additional economic interest. Agriliance s earnings are split among the members based upon the respective economic interests of each member.

Results of Operations

Comparison of the years ended August 31, 2003 and 2002

General. The Company recorded pretax earnings of $136.5 million in fiscal 2003 compared to pretax earnings of $144.8 million in fiscal 2002, with fiscal 2003 net income of $123.8 million, slightly below fiscal 2002 net income of $126.1 million. These results reflected increased pretax earnings in the Agronomy, Energy and Country Operations and Services segments, offset, however, by decreased pretax earnings in the Grain Marketing and Processed Grains and Foods segments.

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The Agronomy segment generated pretax earnings of $13.5 million for the year ended August 31, 2003 compared to $5.8 million in the prior year. This increase in earnings is primarily attributable to the acquisition of an additional economic interest in the Agriliance crop protection business, as discussed earlier.

The Energy segment generated pretax earnings of $83.5 million during the year ended August 31, 2003 compared with $75.8 million during the prior year. This increase in earnings is primarily attributable to strong refining margins. Because agricultural use of fuels is gradually declining, the Company has introduced initiatives to market greater volumes of refined fuels, propane and lubricants to customers outside its traditional base in the agricultural market. The Company established a record number of new Cenex-branded retail sites during fiscal 2003, with nearly 160 dealerships added or converted to the Cenex brand, and has introduced new lines of lubricant products for use in snowmobiles, all terrain vehicles and marine equipment.

The Grain Marketing segment generated pretax earnings of $3.7 million for the year ended August 31, 2003 compared to $8.1 million in the prior year. A major contributing factor was a decrease in exports of grains and oilseeds as the result of increased prices for U.S. grains and oilseeds resulting from drought in parts of the U.S. crop production area which, along with large crops in certain other grain-exporting countries, put U.S. grains and oilseeds in a non-competitive position in the world export market for most of fiscal 2003. During fiscal 2003 the Company constructed 110-car shuttle train receiving stations in Friona, Texas and Collins, Mississippi, which are located near large-scale cattle and poultry producers, with a goal of increasing the volume of domestic grain sales, in part to reduce the Company s exposure to volatile export markets.

The Country Operations and Services segment generated pretax earnings of $32.8 million for the year ended August 31, 2003 compared to $24.1 million for the prior year. This increase resulted primarily from $10.9 million received in cash from a class action lawsuit alleging illegal price fixing against various feed vitamin product suppliers, partially offset by impairments related to facilities where the undiscounted projected income and related cash flows were less than the carrying value of the facilities.

The Processed Grains and Foods segment generated pretax earnings of $4.2 million for the year ended August 31, 2003 compared to $32.2 million for the prior year. This decrease was the result of several factors, most significantly the decrease in CHS s equity income from its investment in Ventura Foods discussed below under Equity Income from Investments, depressed soybean meal prices and margins through much of the year, the effects of the recent shifting of U.S. dietary preferences from carbohydrates to high protein and the impact of restructuring efforts in the Company s Mexican foods operations. These factors were partially offset by the effect of higher prices for refined soybean oil and improved results from the Company s wheat milling operations, in part because of impairment charges recognized in fiscal 2002. In late fiscal 2003, margins at both Ventura Foods and Horizon Milling began to improve.

Net Income. Consolidated net income for the year ended August 31, 2003 was $123.8 million compared to $126.1 million for the year ended August 31, 2002, which represents a $2.3 million (2%) decrease. This decrease in profitability is primarily attributable to decreased earnings in the Company s Processed Grains and Foods and Grain Marketing segments, which was partially offset by increased earnings within the Energy, Country Operations and Services and Agronomy segments compared to the year ended August 31, 2002.

Net Sales. Consolidated net sales of $9.3 billion for the year ended August 31, 2003 increased $2.1 billion (30%) compared to the year ended August 31, 2002.

Company-wide grain and oilseed net sales of $4.5 billion increased $1.0 billion (30%) during the year ended August 31, 2003 compared to the year ended August 31, 2002. Sales for the year ended August 31, 2003 were $4,139.2 million and $1,140.0 million from Grain Marketing and Country Operations and Services segments, respectively. Sales for the year ended August 31, 2002 were $3,281.5 million and $862.0 million from Grain Marketing and Country Operations and Services segments, respectively. The Company eliminated all intersegment sales between Country Operations and Services and Grain

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Marketing, of $799.4 million and $685.4 million, for the years ended August 31, 2003 and 2002, respectively. The net increase in sales was primarily due to an increase of $0.93 (30%) per bushel in the average sales price of all grain and oilseed marketed by the Company while volumes remained essentially unchanged from the prior year. The net increase in company-wide grain and oilseed of $1.0 billion was primarily related to the price change due to stronger commodity prices and increased international soybean exports.

Energy net sales of $3.6 billion increased $963.6 million (37%) during the year ended August 31, 2003 compared to the year ended August 31, 2002. Sales for the year ended August 31, 2003 and 2002 were $3,648.1 million and $2,657.7 million, respectively. The Company eliminated all intersegment sales from Energy to Country Operations and Services of $94.2 million and $67.4 million for the years ended August 31, 2003 and 2002, respectively. Refined fuels net sales increased by $783.2 million, of which $418.0 million was related to a net average price change and $365.2 million was related to a net volume change. The sales price of refined fuels increased $0.18 per gallon and volume increased 17% compared to the year ended August 31, 2002. Refined fuels commodity prices increased due to global uncertainty in the energy markets brought on by the ensuing war and the Venezuela disruption. Propane net sales increased by $137.0 million, of which $75.9 million was related to a net volume change and $61.1 million was related to a net average price change. The average sales price of propane increased by $0.09 per gallon and volume increased by 19% compared to the year ended August 31, 2002. Domestic propane inventories were at extremely low levels coming out of the heating season, which supported a higher selling price. Refined fuels and propane volume increases were primarily a result of acquisitions, with the largest acquisition taking place in November 2001, when the Company purchased for $32.6 million, the wholesale energy business of Farmland Industries, Inc. (Farmland), as well as all interest in Country Energy, LLC a joint venture formerly with Farmland.

Country operations non-grain net sales of $745.8 million increased by $133.3 million (22%) during the year ended August 31, 2003 compared to the year ended August 31, 2002. The net average price and net volume increased on the majority of farm supply products, which consists of seed; plant food; energy products; animal health ingredients, supplements and products; animal health products; and crop nutrient and crop protection products, compared to the prior year. In addition, net sales increased $46.4 million compared to the prior year due to the acquisition of a sunflower processing plant.

Processed Grains and Foods segment net sales of $491.2 million decreased $4.3 million (1%) during the year ended August 31, 2003 compared to the year ended August 31, 2002. Intersegment sales of $0.7 million and $0.6 million for the years ended August 31, 2003 and 2002, respectively, have been eliminated. Oilseed processing and refining net sales increased $81.4 million primarily due to an average selling price increase of $0.07 per pound in refined oilseed. In addition, Mexican Foods sales increased $4.1 million compared to the prior year. These sales increases were partially offset by an $89.6 million decrease in sales due to the formation of Horizon Milling, a wheat flour milling and processing joint venture that was formed in January 2002. After that date, the Company accounted for operating results of Horizon Milling under the equity method of accounting.

Patronage Dividends. Patronage dividends received from other cooperatives of $3.3 million decreased $0.6 million (16%) during the year ended August 31, 2003 compared to the year ended August 31, 2002 from cooperatives of which CHS is a member and with which it does business. The amount of patronage dividends received by CHS in each year depends on the volume of business CHS conducted with the other cooperative (which, in turn, depends on how the terms offered by that cooperative compare to the terms offered by other entities), the profitability generated by the other cooperative on the product purchased by or from CHS, and the patronage distribution resolution adopted by that other cooperative for that year. All of these factors vary from year to year.

Other Revenues. Other revenues of $124.5 million increased $15.1 million (14%) during the year ended August 31, 2003 compared to the year ended August 31, 2002. The majority of other revenue was generated within the Country Operations and Services and the Grain Marketing segments and derived primarily from services performed through the Country Operations and Services segment s elevator and

agri-service centers, including grain storage, grain cleaning, fertilizer spreading, crop protection product spraying and other services of this nature; the Country Operations and Services segment s financial services; and the Grain Marketing segment s service activities at its export terminals for loading vessels.

Cost of Goods Sold. Cost of goods sold of $9.1 billion increased $2.1 billion (31%) during the year ended August 31, 2003 compared to the year ended August 31, 2002. The cost of all grains and oilseed procured by the Company through its Grain Marketing and Country Operations and Services segments increased 30% compared to the year ended August 31, 2002 primarily due to a $0.92 (30%) average cost per bushel increase while volumes remained essentially unchanged from the prior year. This increase in cost of goods sold was primarily the result of higher commodity prices and increased international exports. The Energy segment cost of goods sold increased by $986.6 million (40%) during the year ended August 31, 2003 compared to the prior year, primarily due to refined fuels average cost increase of $778.1 million (46%), which consists of increased average cost of $0.18 per gallon and volume increases of 17% compared to the year ended August 31, 2002. In addition, the average cost of propane increased by $138.1 million (43%), of which the average cost increased by $0.10 per gallon and volumes increased by 19% compared to the prior year. Energy cost increases were primarily related to the global effects of higher input costs and increased volumes primarily as a result of acquisitions. Country operations non-grain cost of goods sold increased by 12% during the year ended August 31, 2003 compared to the prior year primarily due to a sunflower processing plant acquisition and increased average cost per unit on most farm supply products. Processed Grains and Foods segment cost of goods sold increased by $9.3 million (2%) compared to the year ended August 31, 2002. Oilseed processing and refining cost of goods sold increased $94.6 million, primarily due to the increased cost of raw materials related to oilseed refining of $0.07 per bushel. This increase was partially offset by decreased cost of goods sold of $89.7 million related to the formation of Horizon Milling, as previously discussed.

Marketing, General and Administrative. Marketing, general and administrative expenses of $190.6 million for the year ended August 31, 2003 increased by $3.3 million (2%) compared to the year ended August 31, 2002. The net increase is primarily due to additional expenses within the Country Operations and Services segment primarily due to a sunflower plant acquisition.

Gain on Legal Settlements. The Country Operations and Services segment received cash of $10.9 million and $3.0 million during the years ended August 31, 2003 and 2002, respectively, from a class action lawsuit alleging illegal price fixing against various feed vitamin product suppliers.

Interest. Interest expense of $48.7 million for the year ended August 31, 2003 increased by $6.2 million (15%) compared to the year ended August 31, 2002. The average level of short-term borrowings increased $88.1 million primarily due to financing working capital needs, which was partially offset by an average short-term interest rate decrease of 0.4% during the year ended August 31, 2003 compared to August 31, 2002. Long-term debt borrowings increased due to an additional $175.0 million of private placement debt that was issued in October 2002.

Equity Income from Investments. Equity income from investments of $47.3 million for the year ended August 31, 2003 decreased by $10.8 million (19%) compared to the year ended August 31, 2002. The Company records equity income or loss from the investments it owns 50% or less of for its proportionate share of income or loss reported by the entity, without consolidating the revenues and expenses of the entity in the Company s consolidated statements of operations. The decrease in equity income from investments was primarily attributable to decreased earnings in Ventura Foods, which was partially offset by increased earnings in Agriliance compared to the prior year. Equity earnings in Ventura Foods decreased $16.2 million during fiscal 2003 when compared with earnings of the previous year. This decrease was mostly attributable to higher priced refined soybean oil, which is a primary ingredient in many of Ventura Foods products, and also to the fact that the depressed U.S. economy reduced business for many of Ventura Foods restaurant customers, in turn decreasing demand for and margins on certain of Ventura s products. Equity earnings in Agriliance increased $6.8 million during fiscal 2003 when compared with the previous year. This increase was primarily attributable to the Company s acquisition of an additional 13.1% of economic interest in the wholesale CPP business of Agriliance, as previously discussed.

Minority Interests. Minority interests of $22.0 million for the year ended August 31, 2003 increased by $6.6 million (43%) compared to the year ended August 31, 2002. The net change in minority interests during the year ended August 31, 2003 compared to the prior year was primarily a result of more profitable operations within the Company s majority-owned subsidiaries. Substantially all minority interests relate to National Cooperative Refinery Association (NCRA) an approximately 74.5% owned subsidiary.

Income Taxes. Income tax expense of $12.7 million for the year ended August 31, 2003 compares to $18.7 million for the year ended August 31, 2002, resulting in effective tax rates of 9.3% and 12.9%, respectively. The federal and state statutory rate applied to nonpatronage business activity was 38.9% for the years ended August 31, 2003 and 2002. The income taxes and effective tax rate vary each year based upon profitability and nonpatronage business activity during each of the comparable years.

Comparison of the years ended August 31, 2002 and 2001

Net Income. Consolidated net income for the year ended August 31, 2002 was $126.1 million compared to $178.6 million for the year ended August 31, 2001, which represents a $52.5 million (29%) decrease. This decrease in profitability is primarily attributable to a tax benefit of $34.2 million in the prior year and decreased earnings in the Company s Energy segment compared to the year ended August 31, 2001.

Net Sales. Consolidated net sales of $7.2 billion for the year ended August 31, 2002 decreased $307.8 million (4%) compared to the year ended August 31, 2001.

Company-wide grain and oilseed net sales of $3.5 billion increased $29.0 million (1%) during the year ended August 31, 2002 compared to the year ended August 31, 2001. Sales for the year ended August 31, 2002 were $3,281.4 million and $862.0 million from Grain Marketing and Country Operations and Services segments, respectively. Sales for the year ended August 31, 2001 were $3,416.2 million and $913.4 million from Grain Marketing and Country Operations and Services segments, respectively. The Company eliminated all intersegment sales from Country Operations and Services to Grain Marketing, of $685.4 million and $900.6 million, for the years ended August 31, 2002 and 2001, respectively. The net change in sales was primarily due to an increase of $0.28 per bushel (10%) in the average sales price of all grain and oilseed marketed by the Company, which was partially offset by a decrease in grain volume of 8% compared to the prior year. The net increase in company-wide grain and oilseed of $29.0 million was primarily related to an average price increase of $335.8 million, which was partially offset by a $306.8 million decrease related to volume.

Energy net sales of $2.6 billion decreased $119.1 million (4%) during the year ended August 31, 2002 compared to the year ended August 31, 2001. Sales for the year ended August 31, 2002 and 2001 were $2,657.7 million and $2,781.2 million, respectively. The Company eliminated all intersegment sales from the Energy segment to Country Operations and Services segment of $67.4 million and $71.8 million for the years ended August 31, 2002 and 2001, respectively. Prior to December 31, 2000 the company consolidated the business activity of Cooperative Refining LLC (CRLLC), a refining joint venture into the Energy segment. The Company held a 58% interest in CRLLC, which was dissolved effective December 31, 2000. Energy sales decreased by $371.6 million primarily due to this dissolution. Refined fuels net sales that were not part of CRLLC increased by $259.5 million due to a net volume increase of $575.6 million, which was partially offset by a $316.1 million decrease due to the price change compared to the previous year. These refined fuels sales volumes increased by 49%, which was partially offset by a decrease of $0.21 in the average selling price compared to August 31, 2001. Propane net sales decreased by $35.0 million; $109.7 million due to the decrease in net price, which was partially offset by a $74.8 million increase due to net volume change. The average sales price of propane decreased by $0.21 per gallon, which was partially offset by volume increases of 28% compared to the year ended August 31, 2001. Refined fuels and propane volume increases were primarily a result of acquisitions, with the most substantial acquisition taking place in November 2001, when the Company purchased for $32.6 million, the wholesale energy business of Farmland Industries, Inc. (Farmland), as well as all interest in Country Energy, LLC a joint venture formerly with Farmland.

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Country operations non-grain sales of $612.5 million decreased by $51.3 million (8%) during the year ended August 31, 2002 compared to the year ended August 31, 2001. The decrease is primarily due to a reduction of $46.3 million (24%) in the average retail sales price of energy products compared to the prior year. Non-grain sales consist of seed; plant food; energy products; animal health ingredients, supplements and products; animal health products; and crop nutrient and crop protection products.

Processed Grains and Foods segment net sales of $495.5 million decreased $166.4 million (25%) during the year ended August 31, 2002 compared to the year ended August 31, 2001. Intersegment sales of $0.6 million and $0.8 million, for the years ended August 31, 2002 and 2001, respectively, have been eliminated. Sales decreased $167.4 million primarily due to the formation of Horizon Milling as previously discussed.

Patronage Dividends. Patronage dividends received of $3.9 million decreased $2.1 million (35%) during the year ended August 31, 2002 compared to the year ended August 31, 2001, due to reduced patronage dividends from cooperatives.

Other Revenues. Other revenues of $109.5 million decreased $6.8 million (6%) during the year ended August 31, 2002 compared to the year ended August 31, 2001. The majority of other revenue was generated within the Country Operations and Services and the Grain Marketing segments and derived primarily from services performed through the Country Operations and Services segment s elevator and agri-service centers, including grain storage, grain cleaning, fertilizer spreading, crop protection product spraying and other services of this nature; the Country Operations and Services segment s financial services; and the Grain Marketing segment s service activities at its export terminals for loading vessels.

Cost of Goods Sold. Cost of goods sold of $6.9 billion decreased $240.5 million (3%) during the year ended August 31, 2002 compared to the year ended August 31, 2001. The cost of all grains and oilseed procured by the Company through its Grain Marketing and Country Operations and Services segments increased $28.0 million compared to the year ended August 31, 2001 primarily due to a $0.27 (10%) average cost per bushel increase, which was partially offset by an 8% decrease in volume. This increase was partially offset by decreases in cost of goods sold in the Processed Grains and Foods, Country Operations and Services and Energy segments. Processed Grains and Foods segment cost of goods sold decreased by 26% compared to the year ended August 31, 2001, primarily due to the formation of Horizon Milling, as previously described. Country operations non-grain cost of goods sold decreased by 9% during the year ended August 31, 2002 compared to the prior year primarily due to the reduced cost of energy products. The Energy segment cost of goods sold decreased by 2% during the year ended August 31, 2002 compared to the prior year, primarily due to the dissolution of CRLLC, as previously discussed. However, the volumes of refined fuels that were not associated with the dissolution of CRLLC increased by 49%, which was partially offset by an average cost decrease of $0.18 per gallon compared to the year ended August 31, 2001. The average cost of propane decreased by $0.19 per gallon, which was partially offset by a 28% volume increase compared to the prior year. These volume increases were primarily the result of acquisitions.

Marketing, General and Administrative. Marketing, general and administrative expenses of $187.3 million for the year ended August 31, 2002 increased by $3.2 million (2%) compared to the year ended August 31, 2001. The net increase is primarily due to additional expenses resulting from Energy segment acquisitions, which was partially offset by reduced expenses within the Processed Grains and Foods segment due to the formation of Horizon Milling described earlier.

Gain on Legal Settlements. During the fiscal year ended August 31, 2002, the Country Operations and Services segment received $3.0 million in cash from a class action lawsuit alleging illegal price fixing against various feed vitamin product suppliers.

Interest. Interest expense of $42.5 million for the year ended August 31, 2002 decreased by $19.0 million (31%) compared to the year ended August 31, 2001. The average level of short-term borrowings decreased $68.3 million (24%) and the average short-term interest rate decreased 3.6% during the year ended August 31, 2002 compared to the prior year. The net decrease in interest expense from

short-term borrowings was partially offset by an increase due to an additional $80.0 million of long-term debt from a private placement, of which $25.0 million and $55.0 million were issued in January and March 2001, respectively.

Equity Income from Investments. Equity income from investments of $58.1 million for the year ended August 31, 2002 increased by $29.6 million (104%) compared to the year ended August 31, 2001. The increase was primarily attributable to decreased losses from Corporate and Other segment technology investments of $15.1 million which was dissolved. In addition, earnings from Agronomy, and Processed Grains and Foods segments investments increased in fiscal year 2002 by $6.1 million and $5.8 million, respectively compared to the prior year.

Minority Interests. Minority interests of $15.4 million for the year ended August 31, 2002 decreased by $19.7 million (56%) compared to the year ended August 31, 2001. The change in minority interests during the year ended August 31, 2002 compared to the prior year was primarily a result of less profitable operations within the Company s majority-owned subsidiaries and the dissolution of CRLLC. Substantially all minority interests relate to National Cooperative Refinery Association (NCRA) an approximately 74.5% owned subsidiary.

Income Taxes. Income tax expense of $18.7 million for the year ended August 31, 2002 compares to a tax benefit of $25.6 million for the year ended August 31, 2001, resulting in effective tax rates of a 12.9% expense and a 16.7% benefit, respectively. The federal and state statutory rate applied to nonpatronage business activity was 38.9% for the years ended August 31, 2002 and 2001. An income tax benefit of $34.2 million for the year ended August 31, 2001 resulted from a change in the tax rate applied to the Company s cumulative temporary differences between income for financial statement purposes and income used for tax reporting purposes. The Company s calculation of its patronage distribution using earnings for financial statement purposes rather than tax basis earnings prompted the rate change. The Company recorded income tax expense of $18.7 million for the year ended August 31, 2002, which compares to $8.6 million for the year ended August 31, 2001, exclusive of the $34.2 million benefit related to the change in patronage determination described above. The income taxes and effective tax rate vary each year based upon profitability and nonpatronage business activity during each of the comparable years.

Liquidity and Capital Resources

On August 31, 2003 the Company had working capital, defined as current assets less current liabilities, of $458.7 million and a current ratio, defined as current assets divided by current liabilities, of 1.3 to 1.0. Included in this working capital was $168.2 million of cash and cash equivalents. On August 31, 2002, the Company had working capital of $249.1 million and a current ratio of 1.2 to 1.0 and on August 31, 2001, the Company had working capital of $305.3 million and a current ratio of 1.3 to 1.0. During fiscal 2003, the Company borrowed $175.0 million from a group of insurance companies on a long-term basis and also received net proceeds of $82.5 million from the sale of preferred stock to the general public. These sources contributed significantly to the increase in the amount of the Company s working capital during fiscal 2003. The Company raised this additional capital in part to fund capital expenditures that it made in fiscal 2003 and expects to make in fiscal years 2004 and 2005 to meet the new low sulfur fuel regulations discussed below in Cash Flows from Investing Activities. The Company has committed lines of revolving credit totaling $730.0 million, of which $250.0 million was drawn on August 31, 2003, primarily for the purpose of financing receivables and inventories. These receivables and inventories are highly liquid. The Company believes that its liquidity is adequate to cover any increase in net operating assets and liabilities.

Cash Flows from Operations

Cash flows from operations are generally affected by commodity prices. These commodity prices are affected by a wide range of factors beyond our control, including weather, crop conditions, drought, the availability and adequacy of supply and transportation, government regulations and policies, world events, and general political and economic conditions. These factors, which are described in greater detail in this

Form 10-K/A-1 under the heading Business Cautionary Statement Regarding Forward-Looking Statements, may affect net operating assets and liabilities and liquidity.

Cash flows provided by (used in) operating activities were $216.5 million, ($35.9) million, and $253.9 million for the years ended August 31, 2003, 2002 and 2001, respectively. Volatility in cash flows from operations for the years ended August 31, 2003, 2002 and 2001 was caused primarily by fluctuations in the year-end price of spring wheat, soybeans and corn, our highest volume commodities. Although crude oil prices have experienced volatility during the three-year period, values on August 31, 2003, 2002, and 2001 were comparable, thus not contributing significantly to changes in net operating assets and liabilities on those dates.

Operating activities of the Company provided net cash of $216.5 million during the year ended August 31, 2003. Net income of $123.8 million and net non-cash expenses of $98.0 million were partially offset by a small increase in net operating assets and liabilities requirements of $5.3 million. The primary components of net non-cash expenses included depreciation and amortization of $111.3 million which was partially offset by net income from equity